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IN THE

Supreme Court of the United States

OCTOBER TERM, 1946

No. 501

THE OKONITE COMPANY,
Petitioner,

v.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE THIRD CIRCUIT.

MOTION FOR REHEARING.

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ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE THIRD CIRCUIT.

MOTION FOR REHEARING.

To the Honorable the Chief Justice and the Associate Justices of the Supreme Court of the United States:

Comes now the petitioner, The Okonite Company, by Edmund S. Kochersperger, its attorney of record, and presents this, its Motion for Rehearing (or Reconsideration) on its Petition for a Writ of Certiorari in the above-entitled cause for the reasons hereinafter stated.

Jurisdiction.

The jurisdiction of this Honorable Court is set out on page 5 of the Petition for a Writ of Certiorari.

On September 14, 1946, the Petition for a Writ of Certiorari to the United States Circuit Court of Appeals for the Third Circuit was filed; and on October 28, 1946, the same was denied by this Honorable Court.

Questions Presented.

The fundamental legal question sought for a review by this Honorable Court is basically the same as in two other cases now pending (October Term, 1946) for consideration by this Honorable Court by the granting of Writs of Certiorari on October 14, 1946 in *Adam A. Adams* v. *Commissioner,* Docket No. 209, and *J. Robert Bazley* v. *Commissioner,* Docket No. 287, both cases being upon petitions relative to decisions in the same Third Circuit.

The decisions in the three cases find consecutive reporting in 155 Fed. (2d) at pages 237 to 246 as to *J. Robert Bazley* v. *Commissioner,* at pages 246 to 248 as to *Adam A. Adams* v. *Commissioner,* and at pages 248 to 254 as to *The Okonite Company* v. *Commissioner.*

The decisions in the cases of *Bazley, supra,* and *Adams, supra,* were rendered by the Third Circuit sitting as *court en banc* comprising five judges, with decisions rendered on the same date, April 16, 1946, and with expression of majority and minority views by the Judges of that Court. The decision in the case of *The Okonite Company, supra,* was rendered two days later (April 18, 1946) by a court comprising three judges, and by a specific reference (155 Fed. (2d) 250) in the opinion to the previous decision in the *Bazley* case, *supra,* the unanimous decision by the Court (in the case of this petitioner, The Okonite Company) would appear to find basis in the doctrine of *stare decisis.*

The facts in all three cases are identical in one aspect, namely, each case involved a financial recapitalization in

the different respective corporations. The facts differ inasmuch as the securities received by stockholders in cases of *Bazley* and *Adams* as something additional to the previous holdings of stock were described as "debentures," whereas in the instance of this petitioner, The Okonite Company, similar additional securities found the description as "preferred stock."

The decisions by The Tax Court and by the Third Circuit hold for the taxability as to the "debentures" received in cases of *Bazley, supra,* and *Adams, supra,* but hold for the nontaxability of the "preferred stock" received in the case of *The Okonite Company, supra.* Neither The Tax Court nor the Third Circuit (in case of *The Okonite Company*) emphasizes the contrary or conflicting conclusions by any attempt at distinction between "debentures" and "preferred stock" in terms of taxable or nontaxable consequences to stockholders by reason of such difference in name for the securities received as additional to the former holding by stockholders.

From counsel's examination of the petitions for writ of certiorari in the cases of *Bazley, supra,* and *Adams, supra,* as to which this Honorable Court has granted the respective writs, counsel deferentially suggests that this Honorable Court appears to have taken jurisdiction for the consideration and the rendition of a final judgment regarding a basic and important question of law—

> Is a corporate recapitalization to be denied the nontaxable consequences under Section 112 of the Internal Revenue Code by force of a finding of fact by The Tax Court that the purpose of the recapitalization was *to benefit the stockholders* in distinction from a *corporate business purpose*?

When the case of *The Okonite Company* was decided in The Tax Court (January 29, 1945), the decision was that of Van Fossan, J. *without any review by the full Court* (see 4 T. C. 618), the petitioner's motion to the presiding judge in The Tax Court for such a review being denied (Record, 2a), and denial also occurred of petitioner's motion addressed to Judge Van Fossan for reconsideration and for correction in findings of fact. (Record, 2a.) Those denials occurred on February 27, 1945. (Record, 2a.) *The day following those denials,* the Tax Court announced its decision in the case of *J. Robert Bazley,* 4 T. C. 897, holding *by a divided court upon review* that the purpose of any recapitalization is crucial to the taxable or the nontaxable results, taxable if to benefit stockholders and nontaxable if for corporate business purpose. At 4 T. C. 907, the name of Judge Van Fossan may be noted as disagreeing with that conclusion of the majority of Tax Court Judges.

Judge Van Fossan *made no specific finding of fact as regards the purpose of the recapitalization* in the instance of his decision against *The Okonite Company,* 4 T. C. 618, although the evidence clearly showed *purpose in terms of benefit to the stockholders,* inasmuch as by the payment of dividend-arrears by preferred stock, the payment of cash dividends thereby could be (and was) resumed to both preferred stockholders and common stockholders alike.

Whether or not the *Bazley* case stood under "review by the court" when Judge Van Fossan rendered his decision against this petitioner on January 29, 1945 does not stand disclosed to the public, but such a review must have been in process on February 27, 1945 (when the two motions were denied in The Tax Court to The Okonite Company), inasmuch as the decision in the *Bazley* case finds rendition on February 28, 1945 (4 T. C. 897).

If the purpose of a corporate recapitalization is crucial to the taxable or the nontaxable results, the same basic question stands in the case of the petitioner as in the cases of *Bazley, supra,* and *Adams, supra,* as to which this Honorable Court has granted certiorari.

Reasons for Granting the Motion and, by Rehearing, for Granting the Writ.

Sufficient reasons for prevention of a grave miscarriage of Justice would appear to find recital under the foregoing subject heading.

That Judge Van Fossan did not make any specific finding of fact regarding the purpose of the recapitalization, where the evidence so clearly showed purpose in terms of benefit to stockholders, most obviously is consistent with his dissenting view finding expression in the *Bazley* case (4 T. C. 897, at 909) that *purpose holds no importance.* But it is not consistent with the majority views expressed respectively by The Tax Court and the Third Circuit in the *Bazley* case, *supra.* (Petitioner's efforts for correction in the Third Circuit proved futile.)

When applying the decision in the *Bazley* case, under the doctrine of *stare decisis,* to the case of petitioner, The Okonite Company, the opinion by the Third Circuit describes as "a statement of corporate purpose" (Record, p. 183) the fact that the dividend-arrearages were "eliminated" by the process of *payment* through the delivery of the preferred stock as additional to the stockholders' previous holdings of stock. Equally, as a corporate purpose in the *Bazley* and *Adams* cases, the capitalization of Surplus into debentures "eliminated" possibility for payment of cash dividends out of Surplus.

It is fundamental in corporate financing that any accumulation of preferred dividends in arrears is *not a corporate liability* finding appearance among liabilities on a balance sheet. It is a *preference* as against the interest and the rights of the *common stockholders*, who may be debarred of any cash dividends being paid to them until the preferred stockholders are satisfied and, upon a corporate liquidation, funds redound to the common stockholders only after such complete satisfaction to the prefered stockholders. Even in any sense of "elimination" as a legal conclusion, the benefit is to the common stockholders, just as the evidence showed in the case of The Okonite Company (Record, pp. 102a, 103a, and 104a) that cash dividends immediately were resumed to the common stockholders, and continued thereafter, and with cash dividends thereafter being paid to all preferred stockholders as well (Record 103a, 104a.)

If the payment of the dividend arrearage in the case of The Okonite Company had been made by debentures, instead of by a new preferred stock, the comparison with facts in the cases of *Bazley*, *supra*, and *Adams*, *supra*, would make identical situations (and exactly opposite conclusions)—with a single difference that there were specific declarations of dividends and charges against surplus earnings in the instance of The Okonite Company (with a decision for nontaxability), whereas the stockholders in the *Bazley* and *Adams* cases experienced taxability even though there were no declarations as dividends and *no* charges against Surplus.

Thus, it impresses counsel that if the decision in the case of The Okonite Company is denied consideration by this Honorable Court, and if the decisions in the *Bazley* and *Adams* cases are affirmed taxpayers in general defi-

nitely will be informed that taxes to stockholders may be avoided by the process of preferred stock payments, whereas taxes could not be avoided by resort to debentures.

Except for the absence of an expressed and definite future maturity date, the preferred stock involved as to The Okonite Company bore similarity to debentures; the stock was redeemable through a sinking-fund by percentage relative to earnings and was callable at the fixed price of $105.00 per share relative to par value of $100.00 per share.

If it should be the decision by this Honorable Court in the *Bazley* and *Adams* cases, *supra*, that the *purpose* of any corporate recapitalization is crucial and controlling as to taxability or nontaxability, then the ends of Justice would necessitate that the case of this petitioner be remanded to The Tax Court for the making of findings of facts as to purpose, consistent with, and supported by, the evidence.

To the ends of Justice aforesaid, it would appear fitting that counsel for this petitioner have the same opportunity for argument before this Honorable Court on the question of the taxability as to dividends paid by preferred stock, by the granting of writ of certiorari in this case, as now stands accorded to counsel for the Commissioner-respondent relative to the taxability as to dividends paid by debentures through the said granting of writ of certiorari in the cases of *Bazley*, *supra*, and *Adams*, *supra*.

The *Bazley* and *Adams* cases were decided by a full bench of five Judges (Circuit Judges Biggs, Maris, Goodrich, McLaughlin and O'Connell). Three of those five Judges agreed that the distribution of the debentures made in the *Bazley* and *Adams* cases was a dividend, taxable as such to the stockholders, for the reason that the distribution was primarily for the benefit of the stockholders.

Circuit Judges Maris and Goodrich dissented because they felt that the presence or absence of a "corporate purpose" is immaterial and that a recapitalization is a tax free reorganization whether it served the interest of the corporation or of the stockholders.

The significant point and the point which may have been overlooked upon the first consideration of this application is that the instant case was argued before and decided by a Court of three Judges (Circuit Judges Biggs, Maris and Goodrich), two of whom were the minority in the *Bazley* and *Adams* cases. The opinion below was written by Circuit Judge Goodrich of this minority.

Thus the minority in the *Bazley* case controlled the decision in the *Okonite* case. Under these circumstances a further inquiry would serve Justice.

Prayer.

WHEREFORE, petitioner prays that its Motion for Rehearing of its Petition for a Writ of Certiorari herein may be granted; and that upon reconsideration, this Honorable Court may vacate its order entered herein on October 28, 1946, and may enter a new order granting the Petition for a Writ of Certiorari in this cause.

Respectfully submitted,

THE OKONITE COMPANY

By EDMUND S. KOCHERSPERGER,
811 Investment Building,
Washington 5, D. C.
Counsel for Petitioner.

Certificate of Counsel.

The undersigned, counsel for petitioner herein, hereby certifies that the foregoing Motion for Rehearing is presented in good faith as the honest opinion of counsel that the subject matter merits consideration by this Honorable Court and that counsel's action is not in any sense motivated by any thought or desire for delay.

EDMUND S. KOCHERSPERGER,
811 Investment Building,
Washington 5, D. C.
Counsel for Petitioner.

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THE OKONITE COMPANY, *Petitioner*,

v.

COMMISSIONER OF INTERNAL REVENUE, *Respondent*.

On Petition for a Writ of Certiorari to the United States Circuit Court of Appeals for the Third Circuit.

MOTION FOR LEAVE TO FILE SECOND PETITION FOR REHEARING AND PETITION THEREON.

EDMUND S. KOCHERSPERGER, *Esq.*,
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PRESS OF BYRON S. ADAMS, WASHINGTON, D. C.

IN THE

Supreme Court of the United States

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COMMISSIONER OF INTERNAL REVENUE, *Respondent.*

On Petition for a Writ of Certiorari to the United States Circuit Court of Appeals for the Third Circuit.

MOTION FOR LEAVE TO FILE SECOND PETITION FOR REHEARING AND PETITION THEREON.

To the Honorable the Chief Justice and the Associate Justices of the Supreme Court of the United States:

COMES Now the petitioner, The Okonite Company, by Edmund S. Kochersperger, its attorney of record, and presents this, its Motion for Leave to File Second Petition for Rehearing out of time, and Petition Thereon, relative to Petition for a Writ of Certiorari heretofore denied.

Jurisdiction.

The jurisdiction of this Honorable Court is set out on page 5 of the Petition for a Writ of Certiorari.

Reasons for Granting the Motion and, by Reconsideration, for Granting the Writ.

For the prevention of counsel's conception of a grave miscarriage of justice, attention is directed to decisions rendered by this Honorable Court on June 16, 1947 in the cases of *J. Robert Bazley* v. *Commissioner,* No. 287, and *Adam A. Adams* v. *Commissioner,* No. 209, for the pertinency of the Opinion to this petitioner's Petition for Certiorari and to this petitioner's Motion for Rehearing, both standing of record within the October Term, 1946 as denied. Presentation of this Motion necessarily was delayed until rendition of said decisions.

The ends of justice would appear to require that this Honorable Court accord reconsideration to the prior denial of this petitioner's Petition for Writ of Certiorari and the denial of said Motion for Rehearing and, upon such reconsideration, to grant the Writ. Accordingly, the petitioner so moves, and for reasons which follow.

The case of this petitioner in The Tax Court was considered and decided by one Judge, without review by that Court *en banc.* That one Judge held that where stockholders received preferred stock to a substantial value determined by that Judge himself at $89.00 per share, there was a recapitalization of a *nontaxable* nature under Section 112.

The effect of that decision was to deny to this petitioner a deduction for dividends-paid credit as to dividends taxable to stockholders, despite the fact that the Commissioner by interpretation of the law in manner similar to the opinion now expressed in the *Bazley* and *Adams* cases, *supra,* previously had ruled that the dividends were taxable to stockholders of this petitioner, collected taxes from the stockholders, and still stands in possession of unre-

funded taxes collected from stockholders on the interpretation that the dividends were taxable to them.

By both our Petition for Certiorari and our Motion for Rehearing we emphasized the pertinency of the *Bazley* and *Adams* cases to our case. The Third Circuit delayed decision in our case until after its decisions in those other cases, rendering decision in our case two days after the others, and referring to the *Bazley* case in the decision rendered against this petitioner. Now that this Honorable Court has decided the *Bazley* and *Adams* cases upon reasoning that differs from the majority opinion by the Third Circuit in those other cases, that reasoning makes decisions in those other cases even more pertinent to the case of this petitioner.

The petitioner's Motion for Rehearing was filed after the Writ of Certiorari had been granted in the *Bazley* and *Adams* cases, with citation therein only by the Third Circuit's decision in *Bazley, Adams,* and *The Okonite Company* (as the petitioner's own case). The late filing of this petition thus is explained by the fact that, after denial of our Motion for Rehearing, we felt powerless to act until decisions had been rendered by this Honorable Court in the *Bazley* and *Adams* cases, deeming that earlier action on our part would be presumptive in face of the denial of our Motion for Rehearing.

Unless correction is made by this Honorable Court by application of the legal principles stated in the opinions in the *Bazley* and *Adams* cases, as now sustaining the Commissioner's collection of taxes from this petitioner's stockholders, the grave injustice will be done of an unauthorized double collection of taxes, in one instance (stockholders) because the dividends were "taxable" and in the other instance (corporation) because the dividends were "nontaxable," *upon the same identical situation as to facts.*

Language from the opinion in the *Bazley* and *Adams* cases as precluding any refunds to the petitioner's stockholders is pertinent to our situation:

> "It was not the purpose of the reorganization provision to exempt from payment of a tax what as a practical matter is realized gain."

The record in this case shows clearly the "realized gain" to substantial amounts as received by all of petitioner's stockholders, and as the basis for the Commissioner's collection of taxes from them. (See Petition for Certiorari, page 3.)

Again, declares the opinion:

> "A 'reorganization' which is merely a vehicle, however elaborate or elegant, for conveying earnings from accumulations to the stockholders, is not a reorganization under Section 112."

And, again, states the opinion:

> "In the case of a corporation which has undistributed earnings, the creation of new corporate obligations which are transferred to stockholders in relation to their former holdings, so as to produce, for all practical purposes, the same result as a distribution of cash earnings of equivalent value, cannot obtain tax immunity because cast in the form of a recapitalization-reorganization."

Those foregoing quotations effectually paraphrase the contentions advanced by this petitioner both in The Tax Court and before the Third Circuit, and with repudiation at those two stages of the litigation.

The record in this case shows votes by the petitioner's Directors "for conveying earnings from accumulations to the stockholders." That record also shows that petitioner had "undistributed earnings, the creation of new corporate obligations which are transferred to stockholders in relation to their former holdings, so as to produce, for all practical purposes, the same result as a distribution of cash earnings of equivalent value." That record shows (page 38a) that the resort to payment of dividends by "new corporate obli-

gations'' was necessitated because (as the President of the Company testified):

> ''We would like to have paid them in cash but we didn't have the cash to pay them in.''

The only apparent difference between this case and the cases of *Bazley* and *Adams, supra*, is that the payment was by preferred stock in our case, while by debentures in the others.

On the basis of the opinion in the *Bazley* and *Adams* case, the Commissioner can find justification for refusing refunds of taxes paid by our stockholders, by acceptance of the reasoning in this new opinion as being a repudiation by this Honorable Court of the opinions expressed in our case by both the single Judge of The Tax Court and the Third Circuit.

Petitioner's counsel would be negligent in his responsibility as a Member of the Bar of this Court, if he failed to address the attention of this Honorable Court to a situation involving a grave miscarriage of Justice, as matters now stand, and to accord opportunity to this Court for correction of the injustice.

All statements in the opinion for the *Bazley* and *Adams* cases characterize the preferred stock dividends in our case as being *taxable dividends*, contrary to the decision by The Tax Court and affirmed by the Third Circuit. By being dividends taxable to our stockholders, it merely is automatic that the dividends-paid credit applies.

If there be any distinction between ''debentures'' as a dividend and ''preferred stock'' as a dividend, that distinction merits consideration by this Court as being a most important legal question where decision is lacking. As matters now stand, the precedents by the three named cases hold the appearance as ''taxable'' when action is by ''debentures,'' but ''nontaxable'' when done by ''preferred stock,'' with the record in our case evidencing our ''preferred stock'' as being practically the same as ''deben-

tures." Unless clarification comes by decision of this Court in petitioner's case, nontaxable reorganizations readily may be arranged through "preferred stock," instead of by "debentures," a result which counsel deems would find disapproval by this Court if considered through the granting of the Writ in our case, but leaving that important question undecided by this Court if the Writ is not granted, while doing a grave injustice to this petitioner.

Prayer.

WHEREFORE, petitioner prays that its Motion for Leave to File Second Petition for Rehearing and Petition Thereon may be granted; and that upon reconsideration, this Honorable Court may vacate prior orders of denial, and may enter a new order granting the Petition for a Writ of Certiorari in this cause.

Respectfully submitted,

THE OKONITE COMPANY,

By: EDMUND S. KOCHERSPERGER,
811 Investment Building,
Washington 5, D. C.,
Counsel for Petitioner.

Certificate of Counsel.

The undersigned, counsel for petitioner herein, hereby certifies that the foregoing Motion is presented in good faith as the honest opinion of counsel that the subject matter merits consideration by this Honorable Court, and that counsel's action is not in any sense motivated by any thought or desire for delay.

EDMUND S. KOCHERSPERGER,
811 Investment Building,
Washington 5, D. C.,
Counsel for Petitioner.